

Message Text

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ACTION ARA-14

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SUBJ: ARELLANO VISIT: MEETING WITH PRIVATE SECTOR LEADERS

REF: LIMA 2276

1. DAS ARELLANO HAD FULL DAY'S SCHEDULE IN LIMA MARCH 16 INCLUDING CALL ON MINISTER OF ECONOMY AND FINANCE, LUNCHEON WITH KEY MEMBERS GOP ECONOMIC TEAM, MEETING WITH GOP NARCOTICS OFFICIALS, AND DINNER WITH LEADERS OF U.S. AND PERUVIAN BUSINESS AND FINANCIAL COMMUNITY. THIS CABLE REPORTS ON THE MEETING WITH PRIVATE SECTOR LEADERS.

2. DCM HOSTED STAG DINNER MARCH 16 FOR BROAD CROSS SECTION OF PERUVIAN AND U.S. PRIVATE SECTOR INDUSTRIAL AND FINANCIAL LEADERS. CHIEF TOPICS OF DISCUSSION WERE ECONOMIC CRISIS, PROSPECTS FOR BUSINESS AND FINANCIAL SECTORS, AND PRIVATE SECTOR CONFIDENCE.

3. THERE WAS GENERAL AGREEMENT THAT ECONOMIC CRISIS WAS SEVERE, MARKED BY RECESSION (ONE BUSINESSMAN ESTIMATED THAT REAL GDP WAS DOWN BY TWO PERCENT LAST YEAR, WHILE
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ANOTHER THOUGHT THAT GDP HAD ABOUT HELD ITS OWN IN 1977), INFLATION (30-40 PERCENT WAS CONSENSUS FOR 1977 WITH 1978 GENERALLY CONSIDERED TO BE AN UNKNOWN QUANTITY BUT WITH THE DANGER THAT INFLATION MAY BE GETTING OUT OF CONTROL), AND CONTINUED DISINCENTIVES FOR DIRECT INVESTMENT, INCLUDING THE LABOR STABILITY LAW UNDER WHICH WORKERS PRACTICALLY CANNOT BE FIRED, THE

LABOR COMMUNITY LAW, AND THE UNAVAILABILITY OF CREDIT. ALL AGREED THAT SHORT-TERM PROSPECTS WERE DIM. NONE THOUGHT THAT 1978 WOULD BE A YEAR OF REAL ECONOMIC GROWTH.

4. ON MEDIUM AND LONG-TERM PROSPECTS, HOWEVER, THE SITUATION WAS NOT SEEN IN SUCH BLEAK TERMS. SEVERAL BUSINESSMEN EXPRESSED THE BELIEF THAT IN THE LONG RUN PERU, WITH ITS RICHNESS IN NATURAL RESOURCES AND TRADITIONALLY STABLE AND PEACEFUL POPULATION, WOULD COME OUT ON TOP. "IF WE SEE ANY LIGHT AT ALL AT THE END OF THE ROAD, WE'LL KEEP ON MOVING TOWARD IT", ONE PERUVIAN INDUSTRIALIST REMARKED. A PERUVIAN BANKER TOLD OF HOW HE AND SOME FRIENDS HAD TWICE BOUGHT PROPERTY TO BUILD A HOTEL IN IQUITOS, ONLY TO HAVE THE PROPERTY EXPROPRIATED. FINALLY, ON THE THIRD ATTEMPT, THEY SUCCEEDED AND THE HOTEL WAS RECENTLY INAUGURATED. OTHERS EXPRESSED SIMILAR DETERMINATION TO PERSEVERE OVER THE COMING YEARS.

5. THERE WAS FRANK CRITICISM OF GOP POLICIES, WITH THE MOST GENERAL COMPLAINT BEING THE LACK OF CREDIT. THOUGH ONE FINANCIAL ADVISOR WHO WAS FORMERLY WITH THE GOVERNMENT DID POINT OUT THAT CREDIT RESTRICTION WAS A KEY PART OF THE IMF STABILITY PROGRAM, THE GENERAL MOOD SEEMED TO BE THAT CREDIT WAS JUST TOO TIGHT AT THE MOMENT. THERE WAS A SHARP DIVISION OF OPINION AS TO LIMITED OFFICIAL USE

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INTEREST RATES, WITH SOME ARGUING FOR AN EARLY MOVE TO POSITIVE INTEREST RATES, WHILE OTHERS ARGUED THAT THIS WOULD BE THE COUP DE GRACE TO MANY FIRMS NOW STRUGGLING WITH THE EFFECTS OF DEVALUATION (INCREASED COSTS OF IMPORTS) AND LACK OF DEMAND.

6. ALL COMPLAINED ABOUT LACK OF DIRECTION BY GOP LEADERS. THEY CITED RECENT PRESSURES FOR FIRMS TO REHIRE WORKERS FIRED FOR PARTICIPATING IN THE ILLEGAL STRIKE OF JULY 19. THEY FAULTED THE GOVERNMENT BUREAUCRACY FOR ITS STRONG ANTI-PRIVATE SECTOR BIAS AND SUFFOCATING RED TAPE. THEY REMARKED THAT TODAY'S CRISIS IS A DIRECT RESULT OF A "REVOLUTION" THAT TRIED TO DO TOO MUCH IN A RELATIVELY SHORT TIME FRAME. NON-PRODUCTIVE INVESTMENTS, NATIONALIZATIONS, AND COSTLY SOCIAL MEASURES, COUPLED WITH INSUFFICIENT INTERNAL SAVINGS, INEVITABLY LED TO OVERDEPENDENCE ON EXTERNAL FINANCING.

7. THERE WAS ALSO SOME DISCUSSION OF THE DEVASTATING EFFECTS ON PERU SHOULD THE COUNTRY "BE FORCED TO DEFAULT". ALL TRANSACTIONS WOULD HAVE TO BE ON CASH BASIS AND THIS WOULD LEAD TO WIDESPREAD BANKRUPTCIES. THIS IN TURN

WOULD CAUSE DOWNFALL OF GOVERNMENT WITH SUBSEQUENT SCRAMBLE FOR POWER. MORE SERIOUS IN LONG RUN WOULD BE PERMANENT DAMAGE TO MILITARY DISCIPLINE AND END TO LEGITIMACY OF ONLY REMAINING PERUVIAN INSTITUTION. PERU WOULD BE VULNERABLE TO EXTERNAL INFLUENCES OF EITHER THE TOTALITARIAN LEFT OR RIGHT AND HUMAN RIGHTS ABUSES WOULD BE COMMONPLACE. THERE WAS A GENERAL FEELING, HOWEVER, THAT THE IMF AND FOREIGN COMMERCIAL BANKS WOULD ASSIST PERU BEFORE SITUATION GOT BEYOND POINT OF NO RETURN, MOTIVATED TO A LARGE EXTENT BY SELF-INTEREST.

8. COMMENT: PERHAPS THE MOST INTERESTING OVERALL IMPRESSION LEFT BY THE PRIVATE SECTOR LEADERS WAS THAT, DESPITE THEIR RECOGNITION OF THE REALITIES OF THE LIMITED OFFICIAL USE

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CURRENT ECONOMIC CRISIS, AND THEIR SCEPTICISM OF THE TALENTS AND EFFECTIVENESS OF THE GOP ECONOMIC TEAM TO DEAL WITH THESE PROBLEMS, THEY NEVERTHELESS RETAIN AN ESSENTIAL ELEMENT OF FAITH IN THE LONG-RANGE FUTURE OF PERU, AND SEEM READY AND WILLING TO UNDERTAKE NEW PROJECTS WHEN OFFERED AN OPPORTUNITY TO DO SO WITH REASONABLE ASSURANCES OF PROFITABILITY. SHLAUDEMAM

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